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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 96-45
Federal-State Joint Board on	)	CC Docket No. 97-160
Universal Service.	)	DA 98-71

COMMENTS OF SPRINT CORPORATION

SPRINT CORPORATION

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May 15, 1998

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SUMMARY

In these comments, Sprint Corporation responds to the universal service plans presented to the Commission on April 27, 1998. Sprint reiterates its belief that any plan adopted by the Commission should be based on five principles including:

- fund support must be based on forward-looking costs;
- there must be a national fund, assessed on both intrastate and interstate retail revenues;
- where a cost-based rate would be prohibitive, a federal benchmark must be established to serve as the maximum affordable local service rate;
- implementation of the plan must be revenue-neutral at its inception (i.e., any LECs experiencing an increase in explicit high-cost funding must make dollar-for-dollar reductions in access charges); and
- contributions to the universal service fund must be recovered from end user customers through a surcharge on all retail services.

Sprint supports the plans proffered by BellSouth, Time Warner and GTE to the extent those plans incorporate these principles.

Sprint disagrees, however, with BellSouth's suggestion that the PICC is an appropriate USF recovery tool. Sprint stresses that, in order for a recovery mechanism to be competitively neutral, it must not permit a carrier group (here the ILEC) to recover its USF contributions from another carrier group. Because the PICC allows the ILEC to recover its USF contributions from the IXC through access charges, the IXC is left paying both its contribution to the fund as well as a major portion of the ILEC's – a far cry from competitive neutrality.

Sprint also disagrees with two elements of GTE's proposal. First, Sprint objects to the notion that federal universal service funds be used to replace

implicit subsidies existing in intrastate rates of any kind. Second, Sprint points out the flaws inherent in GTE's protestations against the use of proxy models and its support of using embedded costs as the basis for determining the cost of service.

Time Warner, like Sprint, urges the Commission to consider the concept of affordability as it establishes a federal affordability benchmark rate. While Time Warner's notion of limiting USF support to households with incomes below the 70th income percentile is economically sound, Sprint is not certain that the plan is administratively workable in the near term. Sprint agrees that, ideally, consumers should pay for the costs of the services they buy, and even in high cost areas, those who can afford to pay cost-based rates should do so. As a first step towards this ideal, USF should be targeted only to low income consumers. Sprint urges the Commission to set the federal benchmark affordable rate at a level that is considerably higher than the average (implicitly subsidized) local service rates that exist today.

Sprint disagrees with those commenters who offered plans based on a variable or sliding benchmark. Only one federal affordability benchmark rate is necessary. To the extent a state finds that rate to be too high, the state may establish its own safety net benchmark rate to work in concert with the federal rate.

Finally, Sprint vehemently disagrees with the proposal put forth by the NARUC Ad Hoc Working Group. Sprint specifically objects to Ad Hoc's suggestions that federal funding be based solely on interstate revenues; that collecting funds from interstate revenues is a progressive manner of collection; that the distribution of subsidy dollars be left to the discretion of individual states; that universal service dollars not be used to reduce interstate access; and that the cost of service be determined on the basis of the lower of embedded or forward-looking costs.

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COMMENTS OF SPRINT CORPORATION

I. INTRODUCTION

On April 27, 1998, numerous parties offered the Commission their proposals for a federal universal service support methodology. In these comments, Sprint offers its observations with respect to those proposals.

In its proposal, Sprint offered five principles upon which any successful universal service proposal must be based. Those principles include:

- fund support must be based on forward-looking costs;
- there must be a national fund, assessed on both intrastate and interstate retail revenues;
- where a cost-based rate would be prohibitive, a federal benchmark must be established to serve as the maximum affordable local service rate;
- implementation of the plan must be revenue-neutral at its inception (i.e., any LECs experiencing an increase in explicit high-cost funding must make dollar-for-dollar reductions in access charges); and
- contributions to the universal service fund must be recovered from end user customers through a surcharge on all retail services.

Underlying all of these principles is the fundamental premise on which they are based – that there will be no meaningful, facilities-based competition until such time as the revenue stream from end users and subsidy sources is predictable, sufficient, and sustainable. The current system of implicit, inefficient, untargeted subsidies is not only unsustainable, it is unlawful, and will not attract competition to the local market. No quantity of corporate mergers will bring true competition to a market where there is no profitability. BellSouth recognizes this truth when it rightly observes[1] that implicit support in interstate access must be replaced by the new universal service fund. Their conclusion is that the new universal service fund should replace not only the existing *explicit* support (high cost dollars, dial equipment minute weighting, long term support),[2] but should also include the existing *implicit* support in interstate access. Sprint agrees. The Telecommunications Act of 1996 requires nothing less.

II. BELLSOUTH PROPOSAL

Sprint also agrees with BellSouth when it suggests the states should be responsible for eliminating any implicit support remaining after the federal fund is implemented. Although the national policy of universal service should be first addressed by a national solution, state augmentation is most appropriate. States should be free to respond to the unique needs of their inhabitants and tailor their own plans if needed within the bounds of explicit and competitively neutral recovery. Some states may feel the federal benchmark (whatever it may

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[1] BellSouth comments, Attachment 1.

[2] ***BellSouth included the Lifeline and Linkup programs in its plan. While Sprint agrees that these programs must be figured in to the new USF plan, because they specifically address low income issues, they should be treated separately from those elements which address high cost issues.***

ultimately be) may not be appropriate for their area. They should be free to respond accordingly. Some states have already addressed implicit intrastate access subsidies, while others have not. The federal plan must allow enough flexibility for the states to react as they see fit, as long as they state plans are consistent with the mandates to promote local competition and to ensure competitive neutrality in any universal service support mechanism.

BellSouth also is on target when it suggests the assessment base for contributions should be the sum of interstate revenues and intrastate revenues. The legal basis has already been established by the Commission.[3] As competition develops, the distinction between interstate and intrastate services and their attendant revenues will become hopelessly blurred. Consequently, calculating a carrier's USF contribution on both interstate and intrastate revenues will lessen administrative burdens and also eliminate incentives for contributors to misreport revenues to avoid their obligations. Moreover, because all carriers would make their contributions on a basis of total revenues, a national fund will meet the policy goals set forth in Section 254 by guaranteeing a fund that is competitively neutral.

The importance of competitive neutrality as a necessary component of the universal service recovery mechanism cannot be stressed enough. The Commission, in its recent order concerning cost recovery for the provision of

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[3] *In the Matter of Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776 (1997).

local number portability,[4] recognized the essential nature of competitive neutrality when it found that:

> We also conclude that section 251(e)(2) requires the Commission to ensure that number portability costs are distributed among, as well as recovered by, carriers on a competitively neutral basis... We find further that reading section 251(e)(2) as applying to both distribution and recovery best achieves the congressional goal of ensuring that the costs of providing number portability do not restrict the local competition that number portability is intended to encourage. Because the manner in which carriers recover the costs of providing number portability could affect their ability to compete, we cannot ensure that number portability costs are "borne by all telecommunications carriers on a competitively neutral basis" unless we address both distribution and recovery. If the Commission ensured the competitive neutrality of only the distribution of costs, carriers could effectively undo this competitively neutral distribution by recovering from other carriers. For example, an incumbent LEC could redistribute its number portability costs to other carriers by seeking to recover them in increased access charges to IXCs. Therefore, we find that section 251(e)(2) requires the Commission to ensure that both the distribution and recovery of intrastate and interstate number portability cost occur on a competitively neutral basis.[5]

Sprint asserts that, in considering the distribution and recovery mechanisms to be applied to universal service funding, Congress, in section 254(d), requires this same competitive neutrality.

Unfortunately, BellSouth misses the mark when it discusses recovery of the contributions to the fund and advocates a primary interexchange carrier charge (PICC). It suggests that "some kind of" PICC likely will be necessary to recover local exchange carrier (LEC) contributions to the fund.[6] As many have

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[4] *In the Matter of Telephone Number Portability*, CC Docket No. 95-116, Third Report and Order rel. May 12, 1998.
[5] *Id.*, at paragraph 39.
[6] BellSouth Comments, Attachment 1 at page 2.

pointed out in this and other proceedings, the convoluted PICC is far from competitively neutral. Because the LEC levies the PICC on the interexchange carrier as part of the LEC's access charges, the interexchange carrier is left with paying for its contribution to the universal service fund and paying for a major portion of the LEC contribution – a far cry from competitive neutrality, as the Commission's just released LNP cost recovery order clearly demonstrates. [7]

The last element in the BellSouth proposal worthy of comment is its suggestion that economic cost of providing service should be calculated for areas no larger than wire centers.[8] Sprint agrees, but would go even farther, because the use of areas even as large as wire centers can lead to distortions of costs. The smaller census block group is a more accurate unit of measure since it allows a granularity of analysis that could be masked in a wire center. With the computing power now available, such detail should not prove burdensome and will lead to the correct signals to the marketplace which will, in turn, enhance the probabilities of competition.

III. GTE PROPOSAL

GTE's proposal is consistent with the Sprint principles in a number of aspects. It too points out the desperate need to eliminate the implicit support generated by interstate access, it also has grasped the economic and policy

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[7] For a more complete discussion of the flaws of the PICC concept, Sprint commends the Commission to its comments filed in *In the Matter of Defining Primary Lines,* CC Docket No. 97-181. Sprint initial comments filed September 25, 1997; reply comments filed October 9, 1997. For convenience, copies of these comments are attached hereto as Exhibit A.

correctness of a national fund based on interstate and intrastate revenues, and it correctly advocates recovery of contributions through an end user surcharge.

However, Sprint disagrees with two significant points in the GTE proposal. First, GTE states the federal plan should be large enough to replace the implicit support generated by intrastate access, toll, and vertical features. Although there are subsidies in most of those rates, those services do not come under the purview of the FCC. Although a student of history may debate the merits of Alexander Hamilton's federalists and Thomas Jefferson's democrat-republicans, such luxury is not afforded those crafting universal service plans. While it is true that subsidies exist in services other than access, Sprint asserts that the first priority of the federal universal service fund must be to eliminate access subsidies. Subsidies that reside in intrastate retail rates should also be removed, but the state commissions should grapple with that task, not this Commission.

GTE also continues its advocacy of embedded cost over proxy models for determination of the cost of service. Sprint disagrees. Although one can build a theoretical case that model X or model Y is too complex or that model X or model Y is flawed, if this country desires both a subsidy system and competition, the subsidy system must utilize costs a potential competitor would incur . An efficient subsidy system cannot use as its baseline the costs of the incumbent. The incumbent's embedded costs will be either higher or lower than those of a

[8] BellSouth Comments, Attachment 1 at page 1.

potential entrant will. If the subsidy system uses the costs of the incumbent, the wrong market signals will be sent to the potential entrants and will either discourage efficient entry that should occur or will artificially attract inefficient entry that should not occur. Neither result is a desirable public policy goal. Clearly, a proxy approach is superior to embedded costs if competition is the goal.

IV. TIME WARNER PROPOSAL

Time Warner, like Sprint, maintains that, during the creation of a universal service support mechanism, it is important that the statutory requirement of "affordability" not be overlooked. Time Warner provides a white paper, which focuses on the definition of affordability. Its study suggests that subscribers in the top 30 percent income bracket are able to pay cost-based rates. Consequently, Time Warner urges policy makers to recognize that universal service support should be limited to households with incomes below the 70th income percentile, completely eliminating any universal service funding for census block groups where the median income is above this level.

Sprint believes that Time Warner's proposal is based on sound economic principles, as Sprint itself has consistently advocated the concept of affordability as the basis for a federal benchmark. However, Time Warner's proposal appears to be aimed at issues previously addressed in connection with the Link-Up and Lifeline programs. Moreover, although in agreement with the theory, Sprint is not convinced the plan is administratively workable. Neither does Sprint believe such a plan could be implemented by the Commission's January 1, 1999 deadline. Therefore, while continuing to maintain the relevance the notion of affordability to USF, Sprint points the Commission to its earlier-stated principles. Subscribers should pay for the service they receive and, therefore, local rates must be allowed to increase to cost.

Ideally, rather than subsidizing a high cost area -- causing both the low income subscriber and the millionaire to benefit equally from universal service contributions -- only those low income subscribers for whom cost-based rates would prove prohibitive should receive subsidized services even in high costs areas. As a practical matter, however, the Commission may have little choice initially but to subsidize service for all consumers in high cost areas above some benchmark rate. In setting this benchmark rate the Commission must not lose sight of the fact that low income programs continue to exist that will provide necessary assistance to low income subscribers regardless of the level of the federal benchmark. Thus, in order to keep the high cost support fund of manageable size and limited to truly high cost areas, it is appropriate to set the federal benchmark at a relatively high level (considerably higher than today's average local rate, which effectively subsidizes the vast majority of local subscribers, including those who reside in areas that are not necessarily high cost).

Regardless of the level of the federal benchmark rate – and stressing again the fact that rate should be based on the actual cost of providing service as opposed to today's subsidized rates – Sprint notes that state commissions would continue to have the opportunity to supplement the national benchmark with their own plans if they believe the federal benchmark level is too high for residents of their state. Coincident with the opportunity to establish a lower state benchmark, of course, is the states' responsibility to develop a mechanism to fund any differences that may result in an explicit, competitively neutral manner. In any event, this Commission should not lose sight of affordability as a key element to a workable universal service plan.

V. OTHER PROPOSALS

Other parties address the notion of a federal benchmark rate, but appear to use the concept as a way to balance state and federal jurisdiction issues. These parties, including the Commissions of Colorado and South Dakota, GTE and US WEST, advocate a plan with variable benchmarks. In essence, such a plan would create at least two (GTE suggests there could be more) benchmark levels. The first would represent the level at which the federal fund would provide a portion of the dollars necessary to fill the gap between the cost of service and the benchmark rate - – the state would be expected to contribute the remaining dollars. The second benchmark would represent that rate above which the federal program would supply 100 percent of the universal service funding.

Sprint contends a sliding scale is not necessary. Ideally, the (national) benchmark affordability rate should be the same for all states with the states having the opportunity to establish a safety net benchmark of their own. However, if a sliding scale of multiple benchmarks were to be employed, that approach must be adjusted to the point where it fully replaces all of the interstate subsides, both explicit and implicit. That is paramount to the success of a revised subsidy system.

Current subsidies are immense. The record, as developed to date, establishes no need to provide federal funding beyond that currently provided (implicitly) by access. If, after removing implicit subsidies in access, some high cost states find they need additional support to maintain affordable local rates, the Commission should consider the matter at that time.

VI. AD HOC WORKING GROUP PROPOSAL

In contrast to those states who advocated variable benchmark options or variable support options, several other states worked together to submit a proposal for the Commission's consideration. Known as the Ad Hoc Working Group (Ad Hoc), these states have crafted a plan that provides for a new federal USF, made up of contributions from carriers' interstate operations only, but which will be administered by the states. The level of support would be established by using the lower of a proxy cost estimate of forward-looking cost and embedded costs, as well as a "hold harmless" amount representing the funding currently received by a state (which the plan guarantees would continue). The level of support would be the greater of either the cost results or the "hold harmless" amount.

The Ad Hoc proposal is flawed in several regards. First, it proposes a funding based solely on interstate revenues. Although understandable coming from the perspective of state commissions, this does not recognize the national nature of the policy, the national nature of the proper solution, or the competitive neutrality principle that would be violated. This concept has been discussed at length earlier in this pleading as well as in other proceedings.

Related to that error in logic is the Ad Hoc assertion that collecting funds from interstate revenues is a progressive manner of collection. Empirical data would point to a less demonstrative conclusion. In reviewing 1995 data collected by PNR & Associates[9] it appears households with annual income under $10,000 spend a monthly average of $16.17 on long distance.[10] Households with annual incomes of $40,000 to $50,000 spend a monthly average of $20.09. Thus, low income households are burdened almost as much as middle income families by the present practice of implicitly using toll rates to subsidize local service. Moreover, because toll and optional services are relatively price elastic,

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[9] Bill Harvesting II Database, created and compiled by PNR & Associates, Inc., 1995. The database includes 10,000 observations of actual expenditure on telecommunications (and other) services. All respondents were residential customers and all expenditure figures are monthly. The sample is statistically representative, appropriately weighted and proportioned so that all results are statistically and econometrically valid.

[10] These expenditures represent the total amount paid to the long distance company by the end-user, taking into account any optional calling plans to which the customer might subscribe

maintaining the rates of these services at artificially high levels in order to subsidize local rates actually causes consumers to pay more than necessary for services valued by both high and low income users. In its zeal to maintain subsidies in local rates, Ad Hoc conveniently overlooks this fact.

The Ad Hoc proposal also places the distribution of subsidy dollars in the hands of the state commissions. Sprint can appreciate the desire of the states to maintain some level of control over universal service funding. However, as we have previously stated, the dollars flowing from the fund should be utilized to replace the existing explicit and implicit subsidies in access. The distribution decision should, therefore, be made before the dollars even begin to flow and, under no circumstances, be a matter of discretion. Even under some iteration of the Ad Hoc Working Group's plan, the size of the federal universal service fund will be determined on a census block group level by calculating the difference between forward looking costs and the benchmark rate. Because the size of the fund will be decided on a CBG basis, logic and fairness dictate that the contents of the fund be distributed on that basis as well. A state must not be permitted to secure universal service funds associated with a high cost CBG and then redirect those monies to unrelated subscribers or services. Similarly, the tenets of competitive neutrality require new entrants to receive the same number of universal service dollars as an ILEC would for serving the same customer. Consequently, to the extent the USF dollars associated with a particular CBG are not available to the new entrant because the state has diverted the monies elsewhere, facilities-based competition in high cost areas will be retarded – if it can survive at all. In the end, the Commission's universal service support mechanism is to be a federal support mechanism; should a state wish to exercise its discretion over universal service-related funding, it is free to establish its own consistent and complementary plan.

This notion that federal universal service funds should be dispensed as states see fit highlights the misguided perspective of the Ad Hoc proposal – its statement[11] that universal service dollars should not be used to reduce interstate access. The Ad Hoc group goes so far as to assert that the fund instead be used to either reduce the subscriber line charge for ratepayers,[12] reduce retail rates or to maintain existing rate levels.[13] Each of these suggestions ignore completely the fact, as outlined in Section 254, that federal universal service funds are to be used to replace implicit subsidies. The Ad Hoc group appears instead to be promoting the use of the funds to reduce rates that are already subsidized and, in many cases, well below cost. Nothing could be more antithetical to the requirements of the Act or the goal of competition.

Finally, the portion of the Ad Hoc proposal that suggests using the lower of embedded or forward-looking costs is seriously flawed in its logic. Although such an approach sounds good in that it appears to lower the amount of requisite

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[11] Ad Hoc Comments at p. 28.
[12] *Id.*, at p. 23.

federal funding, it ignores the marketplace realities of what a competitor would face if it were to enter the market. As the Commission has repeatedly recognized, a competitor would not face embedded costs. A competitor would face forward-looking costs. To reiterate, if competition is to emerge, perhaps even flourish, the market must be allowed to send the correct economic signals.

Sprint's universal service principles recognize the important role states must play in this changing environment and provide state regulators with the flexibility they need to achieve their goals. The Commission should work with the states, but should reject the misguided proposal authored by the Ad Hoc Working Group.

VII. CONCLUSION

The Commission's universal service fund should be national in scope, should be funded by assessing both interstate and intrastate revenues, should be based on forward-looking costs, should be revenue neutral at its inception (only), should be recovered through surcharges on end users, and must replace existing explicit and implicit subsidies. The United States already has a "big" universal service fund. We may not refer to all elements of it as "universal service," but it is big. The explicit portion may not be large, but the implicit portion includes above-cost access rates and artificially high rates for intraLATA toll and many discretionary local services. If this country's public policy makers are serious about competition, leadership is going to have to be exhibited. Some hard

[13] *Id.* at p. 28.

decisions are going to have to be made. Implicit subsidies must be replaced and products must stand on their own merits. All of that can be accomplished, but it will take some politically courageous leadership.

What so many parties seem to forget is that whether the federal universal service fund is large or small, explicit or implicit, utilized in an environment of competition or monopoly, the end user pays. Whether the end user pays through artificially higher access rates, appropriately higher local rates, higher tax rates, or through some other mechanism, the end user pays. Does it not make economic sense and public policy sense to allow end users to actually see what the different services cost?

Sprint encourages the Commission to adopt its principles in crafting the details of the national universal service plan.

Respectfully submitted,
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May 15, 1998

Exhibit A

(see footnote #7)

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 97-181
Defining Primary Lines	)	

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September 25, 1997

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SUMMARY

Because of the costs incurred in administering different SLCs and PICCs for primary and non-primary residential lines, Sprint urges the Commission to consider anew whether it should instead direct recovery of non-traffic-sensitive costs from end-users through a cost-based SLC or, in the alternative, eliminate the distinction between primary and non-primary residential lines and set the SLC and PICC for such lines at the weighted average of the two rates otherwise applicable under the Commission's Access Reform order. However, if the Commission decides to go forward with the primary/non-primary dichotomy for residential lines, Sprint urges it to resolve the issues in the Notice by following one basic principle: keep it simple.

There is no need to change the definition of single-line business. The possibility that a multi-line business will seek to reduce its costs by taking one line each from multiple LECs is remote in view of the administrative costs the business would incur in reviewing and paying separate bills each month for each telephone line.

The easiest way for ILECs to administer the primary/non-primary concept for residential customers is to take existing customer accounts as they are, and presume that the main billing number listed on the account is the primary line unless the customer notifies the LEC to the contrary. With this approach, an account verification letter would need to be sent only to those residential customers having multiple lines on one account; it would not be necessary to try to ferret out whether the same household has lines under different accounts, or whether there are one or more family units at any particular residential address. Customers should be permitted to change their designation either in

writing, by telephone or in person, and thus the Commission should not require paper records of such customer designations.

Where a customer obtains lines both from an ILEC and a CLEC that resells the ILEC's service, it is reasonable to presume that the second line ordered is the non-primary line unless the customer indicates otherwise. If the CLEC informs the ILEC that the customer has designated its CLEC line as its primary line, the ILEC should accept such designation and bill the CLEC (for the SLC) and the IXCs involved (for the PICCs) accordingly.

Although adherence to the rules Sprint proposes should be subject to normal audit and enforcement processes, no new special processes are necessary at this time. The amounts at stake per subscriber are too low to impose such expensive systems unless or until there is evidence of widespread abuse that cannot be addressed by normal enforcement measures. However, each ILEC must verify to its carrier customers the number and types of PICCs being charged for each end user customer.

Finally, Sprint does not see the need for Commission-mandated disclosure to all consumers. Sprint's proposal would require notification only to those consumers that have an account with more than one line, and notifications to other consumers will simply cause needless confusion on their part.